THE CROW BENEFIT: HISTORY AND OPTIONS

an Intern Paper

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The transportation of prairie grains to ports giving access to the world market is one of the most persistent problems in western Canadian history. That this is so is dictated by the simple fact of Canadian geography. The major grain and oil-seed producing area is bounded on all sides by obstacles to easy movement: the United States to the South, the Rocky Mountains to the West, the Arctic tundra and Ocean to the North, and the Canadian Shield to the East. The West and the East are the only viable and acceptable routes and, in both cases, long stretches of difficult, expensive, and unproductive rail lines intervene between the production and market points. The assignment of the costs for this transportation has been a major issue from the time when the Canadian Pacific Railway brought the West into the outside market system. We are now in the midst of one of the periodic flare-ups of the controversy which have been a feature of our political and economic life since the 1880s. In exploring this issue and discussing it with farmers, legislators, and colleagues and in reflecting on it myself, I have found that there is little understanding of the evolution of the problem or the various proposed solutions and their implications. I make no claims of providing a definitive analysis of the issue but hope to synthesize some of the voluminous literature on Western Grain Transportation and outline some of the alternatives currently being discussed.

In the beginning, after the construction of the Canadian Pacific Railway mainline, the rail company was in a position of strength

relative to western farmers. It had an absolute monopoly over grain transportation and the western farmers were few and without much political or economic clout. The costs of running the system were immense given the very small population which consumed goods brought in by the Canadian Pacific Railway and produced the grain which was to be carried out. The government of the day had neither the ability nor the inclination to reduce the rates charged for grain transportation. It was financially committed beyond its resources and, in any case, regarded the West as an economic and political servant of the established central and eastern parts of the country. To our way of thinking and even to that of the western population of the day, this was an unjust attitude. Nonetheless, it is easily understandable; the West was acquired and considerable resources were invested in it for the sole purpose of bolstering the strength of the new nation.

The rates charged to farmers by the Canadian Pacific Railway for grain haulage were certainly high. Between 1886 and 1897 farmers paid between sixty and twenty-nine cents per hundredweight to have grain hauled from Calgary to the Lakehead - at that time the only market point for western grain. The reduction to twenty-nine cents had occurred both as a result of increased traffic and pressure from farmers whose grain was worth little in a depressed world market. At the same time, these farmers were paying high prices for eastern manufactures protected by tariffs and for the transportation of the same by rail. The whole situation led to a good deal of vocal discontent from western farmers.

In 1897 a change occurred which, at the time, was not recognized as significant but which, over the last forty years, has become increasingly controversial. The Kootenay district of British Columbia was extremely rich in ore and the Canadian government wished to safeguard the exploitation and transportation of it from American interests. The Canadian Pacific Railway wished to ensure that it would be the beneficiary of the profitable haulage. The two parties formulated the "Crows Nest Pass Agreement", named for the mountain pass through which the line was to run. In return for a subsidy of $11,000 per mile of track and vast tracts of valuable British Columbia land with timber and mineral rights intact, the Canadian Pacific Railway was to reduce freight rates on a number of commodities including west-bound settlers' effects and east-bound flour and grain. These latter reductions were only three cents per hundredweight, regarded at the time as a sop to farmers' demands and of little significance given the economic climate and the already steadily falling rates. What is more important, however, are the clauses which specified that "no higher rates...shall hereafter be charged by the Company,"[1] and that the government should have a hand in rate regulation. None of these provisions caused the Canadian Pacific Railway any anguish at the time, particularly as further reductions occurred as a result of competition in the next few years.[2] University of Alberta historian David J. Hall writes of this situation:

> Although popular myth has it that the CPR officials were staggered at the government demands and that Sifton had bound the railway hand and foot with his tough terms, the company plainly obtained pretty much the agreement it wanted. It was prepared to let the government take the credit for freight rates which it

believed would have come about sooner or later in any case.[3]

The Crow Rates or ones even lower, as dictated by the market, obtained until the last year of the First World War. During this time the Canadian Northern Railway, one of the companies which was later absorbed into the Canadian National Railway, was founded and the competition between it the the Canadian Pacific Railway helped to keep rates low. In August of 1918, the Crows Nest Pass Agreement was suspended under the War Measures Act in recognition of the rising costs associated with wartime wages.[4] Freight rates on grain and flour remained above Crows Nest Pass Agreement levels until 1922 when the Board of Railway Commissioners restored them to their 1897 levels. It is noteworthy that until 1925, the Canadian Pacific Railway was only bound to keep to the Crow Rate on lines which were built prior to 1897. In 1925 the federal government stopped the discriminatory practice of charging higher rates on newer lines and made the Crow Rates applicable to all lines west of Fort William regardless of company or date of construction. At that time it also got rid of the Crow Rate for settlers' effects and make it applicable to grain and flour only. Two further major changes to the system were instituted by acts of Parliament: in 1927 the Crow Rates were extended to grain and flour destined for Pacific ports and in 1931 to that en route to the port of Churchill. No changes of any significance were made to the system from 1931 to 1967 with the single exception of the addition of rapeseed to Crow Rate protection in 1961.

The railway companies had been able to make a reasonable profit, in spite of rising costs, until about the end of the Second World

War. The rapid increases in the volume of grain carried brought increased efficiency to the system. After 1948, however, the increases in wage and capital costs made the haulage of grain at Crow Rate levels unprofitable.[5] This fact was recognized in the report of the MacPherson Royal Commission in 1961 and again in the Snavely and Hall Commission Reports in the 1970s. Moreover, the railway companies were forced to retain branch lines set up in the horse and buggy days of farm transportation. The original idea had been that no farmer should have to haul grain more than a few miles from his farm to the nearest elevator. As a result, the fully developed western rail system featured stations and elevators every eight to ten miles in the intensively farmed areas.[6] These lines were maintained at government behest, for political reasons, long after good roads and large farm trucks were predominant on the prairies. The system became progressively more costly while revenues remaind the same per unit moved. As a result, lines were poorly maintained, equipment was kept in service long after it should have been replaced, and the system steadily lost efficiency.

The National Transportation Act of 1967 implemented some of the recommendations of the MacPherson Commission. The Crow Rates were retained and all but a very few branch lines were protected but government subsidies to cover maintenance costs on uneconomic lines were instituted. There is little evidence to suggest that the subsidies were used on the branch lines for which they were paid out. In effect, they became commodity subsidies to cover the overall cost of transporting grain across the entire system.[7] In addition, some

equipment costs were picked up by the federal government, provincial governments, and the Canadian Wheat Board all of which purchased hopper cars in order that the efficiency of moving grain to the market ports might be improved[8] and farmers might see some of the benefit of the booming world economy of the 1970s.

By 1980, it was clear that the 1967 system was not a sufficient solution. Subsidy payments reached 170 million dollars and, still, lines were being allowed to fall into disrepair. The government appointed J. C. Gilson to undertake yet another study of the situation. Gilson's report advocated drastic changes to the system. He calculated the Crow Benefit - the difference between the statutory rate and a reasonable market rate - at slightly less than 650 million dollars for 1981/82. He suggested that this should be the government's annual contribution to the system and that it should be paid primarily to producers, after a long transition period, in the form of either cash payments or freight credits. The railway companies should continue to receive a part of this subsidy but should derive their income primarily from increased rates. Cost increases over and above the 1981/82 level due to volume increases should, in Gilson's view, be born by the farmers and those due to inflation should be shared between the government and the farmers. The Gilson recommendations featured a flexible approach to the problem with adjustment boards and periodic reveiws to monitor the development of the new system.

The Gilson proposals sparked a flurry of criticism from producer associations, the Quebec, Manitoba, and Saskatchewan governments,

and the Canadian Wheat Board.[9] They contended that only by paying subsidies to the railways could performance guarantees be enforced and the efficiency of the system improved and that only by maintaining the Crow Benefit to farmers could profitable prairie agriculture survive. The Quebec objections related to the potential harm to the red meat industry of that province which depends on the competitive edge given it by subsidized grain transportation costs. Of the major interested parties, only the Alberta government expressed support for the major principles embodied in the Gilson Report.

The objections were sufficiently vocal that when Bill C-155, the Western Grain Transportation Act, was introduced in 1983, it contained only some of the Gilson recommendations. It accepted the principle that the railway companies should receive a fair rate of return for services provided but provides for this to be done through a subsidy of 651.1 million dollars per year paid entirely to the railways and not the the farmers and by increased rates to be paid by the farmers. Rate increases to the farmers may be as much as six percent during the 1986/87 crop year. The Act also contains a volume cap: only 31.4 million tonnes - the amount of the 1981/82 crop - will be eligible for the subsidized rates, although it extends subsidies to a short list of additional products. The Western Grain Transportation Act contains two provisions which might be termed guarantees. First, subsidy payments can be withheld if a railway company is not seen to be investing sufficient capital for system improvements. Second, the farmers are to be safeguarded from a rising cost/falling market price situation by a safety net feature

which allows the federal government to pick up transportation costs which exceed ten percent of export market price.

Reactions to Bill C-155 were invited by the Government of Canada and were mixed. Most interested parties felt that the proposed legislation was better than the status quo but found it to be less than idyllic.[10] Opposition to the volume cap was virtually universal as it was perceived to be a disincentive to increased production. Most also felt that the list of subsidized products should be extended further and that the railway performance guarantees should be strengthened. Reaction was most varied on the method of payment of the Crow Benefit subsidy. The Wheat Pools, the Manitoba government, and the Saskatchewan Federation of Agriculture all supported payments to the railways for which the bill provided. The governments of Alberta, Saskatchewan, and British Columbia, the grain companies, prairie livestock associations, and some producer associations were in favour of either payment to farmers or a system which allowed individual farmers to choose payment to themselves or to the rail companies in exchange for subsidized rates - a slight variation of the Gilson proposal. A few other ideas were advanced: public equity in exchange for subsidy and a scheme which allowed producers a specific freight entitlement.

In spite of significant negative western reaction to Bill C-155 and considerable agreement on desireable areas for change, it was passed through the Parliament of Canada with few alterations and the Western Grain Transportation Act came into effect January 1, 1984.

In spite of the implementation of the Western Grain Transpor-

tation Act, the debate regarding the method of payment of the Crow Benefit continues. In part, this is a result of the change of government in Ottawa. There is some feeling that the Conservative administration may be more responsive to those who are asking for direct payment, or some hybrid version thereof, to the farmers. This issue is worthy of further exploration; the two major alternatives - payment to the producer and payment to the railways - could have widely differing effects on the development of the agriculture industry and the transportation network in Canada. Yet, it must be recognized that neither offers a perfect solution to the problem; both have inherent problems and even dangers.

The need for a subsidy is not seriously questioned by anyone. If our agricultural products are to be competitive in the world market, given our geographic disadvantages and the subsidization policies of many of our competitors, then we must retain the Crow Benefit in some form. It is clearly in the national interest to support our agricultural sector. The value of western Canadian agricultural exports was 7.386 billion dollars in 1984, approximately 67.2 percent of total Canadian agricultural exports and 6.7 percent of total Canadian exports of all kinds.[11] It is apparent, therefore, that western Canadian agriculture contributes significantly to our balance of trade position. Moreover, the value of spin-off benefits from agriculture in the domestic economy of western Canada are unparallelled by any other industry.

The system which we have at present of paying the Crow Benefit subsidy to the railway companies offers some definite advantages.

It is well recognized that the rail system in Canada needs significant investment if it is to operate at a level of efficiency sufficient to move prairie grain to market. Direct payments to the railways allow the federal government to demand and enforce performance guarantees for track and equipment improvements. The criticism leveled against this argument, that the federal government has not used its leverage in this area to its full extent,[12] does not alter the fact that it has the option to do so. Direct payments have the further advantage of administrative simplicity and, therefore, cost efficiency. There is an attitude within the political realm which might be characterized as, "better the devil you know." There is a reluctance to make drastic changes because of the chance that they will fail utterly.

The major argument against direct payment of the subsidy to the railway companies is that it distorts the market and hampers the development of agricultural processing in the West. If grain is produced in western Canada and shipped at subsidized rates to, for example, Quebec, then livestock producers in that province can raise an animal which has a lower export market point price than one raised in Alberta and shipped at non-subsidized rates to the export market point. The same argument holds true for value-added processing of grains and oil-seeds. The marketing options of western farmers are seriously limited by direct payments of subsidies to the railways. There is little incentive for them to explore alternative domestic uses for their products in a system which is geared to exporting grain out of the region and out of the country.

The other solution to the subsidy question - payment of the dif-

ference between the statutory freight rates for grain and a reasonable regulated market rate directly to the farmer in the form of cash or freight rate credits while allowing rail companies to charge full price for service rendered - has been championed by the Government of Alberta along with many of the other interested parties. The major argument in favour of this scheme is that it would create more opportunity for the development of a stronger livestock and a value-added processing industry in the West. It is undeniably true that the system of payment to the railway companies acts as a disincentive to this type of development. However, there are those who, like the Government of Manitoba, argue that a change in the method of payment of Crow Benefit subsidies would not be enough to prompt the growth of secondary agricultural industries in the West. They claim that the governments of Ontario and Quebec and the federal government would never allow the processing and livestock industries of central Canada to be superseded by the development of new ones in the West.[13] The veracity of either the Alberta or the Manitoba claim has yet to be tested. Certainly, however, the payment of the subsidy to the farmers would not in any way harm the chances of those industries on the prairies.

Other agruments in favour of this method of payment have been advanced by the Alberta government. The efficiency of the grain handling system would likely see some improvement. At present, there is no benefit to the farmer in allowing the consolidation of elevator facilities; in fact, there is a considerable disincentive to do so.[14] Rail transportation is subsidized but no other form of

transportation is. Therefore, farmers as a group will continue to press for the maintenance of branch lines. If, however, there was individual benefits to be gained by them in creating the most cost efficient grain handling system and transportation was subsidized whatever the mode, there would be more incentive to have consolidated elevators and utilize trucking facilities and varied forms of consolidating shipments. The Alberta government also contends that payment of the Crow Benefit subsidy to farmers would improve cash flow and net farm income substantially[15] and would, therefore, improve the economy of the prairie provinces.

One should not paint too rosy a picture of the payment-to-producers scenario. As indicated earlier, it too has some problems. There is a danger that western Canadian agricultural products might face additional tariff barriers because consumer nations might perceive Crow Benefits to farmers as a commodity rather that a transportation subsidy. Our recent experience with the tightening of the American market to Canadian hogs has demonstrated that this could be a serious problem. There is also a problem with ensuring that the railways respond to agricultural needs. A system featuring payment of the subsidies to farmers depends on market forces to ensure that railways give adequate and efficient service. It may be that this will be sufficient but there is evidence to suggest that grain will form a decreasing percentage of railway business as the production of other commodities, particularly coal, is on the increase.[16] It may well be, therefore, that without performance guarantees the railway companies will shift their priorities away from

grain handling.

Obviously there are problems and advantages to be gained regardless of the method of payment which is adopted. In choosing to continue payments to the railways, the federal government selected the most tested and safest option. It may well be, however, that they failed to choose the best option. Certainly this is the opinion of the Economic Council of Canada.[1] Given that the Gilson scheme of direct payments to producers or some variant thereof has never been tested, it is impossible to come to any definitive conclusions.

ENDNOTES

[1]Hall, p. 155.

[2]Byron, p. 5.

[3]Hall, p. 155.

[4]Government of Canada, Hall Commission, p. 37.

[5]Schweitzer, p. 70.

[6]Ibid, p. 69.

[7]Government of Canada, Hall Commission, p. 59.

[8]Schweitzer, p. 72.

[9]Byron, pp. 15-24.

[10]Macmillan, pp. 10-13

[11]Telephone conversation with the Alberta Agriculture Statistics Branch, June 25, 1985.

[12]Alberta Economic Development and Alberta Agriculture, p. 6.

[13]Byron, p. 17.

[14]Government of Alberta, pp. 18-19.

[15]Ibid, p. 14.

[16]Byron, p. 9.

[17]Schweitzer, pp. 83-84.

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